

STATE OF MINNESOTA  
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

In the Matter of the Application  
of Farmers and Merchants Bank of  
Balaton, Minnesota to Establish  
a Detached Facility in North Mankato,  
Minnesota.

FINDINGS OF FACT,  
CONCLUSIONS AND  
RECOMMENDATION

The above-entitled matter came on for hearing before Administrative Law Judge George A. Beck, on December 18, 1990 at the North Mankato Municipal Building, in the City of North Mankato, Minnesota.

William T. O'Connor, Esq., of the firm of Berens, Rodenberg & O'Connor, 519 Center Street, New Ulm, Minnesota 56073, appeared representing the Applicant, the Farmers and Merchants State Bank of Balaton. Keith Boleen, President, Valley National Bank, 245 Belgrade Avenue North, Mankato, Minnesota 56001, appeared on behalf of the Objector, the Valley National Bank of North Mankato. The record closed on the date of the hearing, December 18, 1990.

This Report is a recommendation, not a final decision, the Commissioner of Commerce will make the final decision after a-review of the record which may adopt, reject or modify the Findings of Fact, Conclusions, and Recommendations contained in this Report. Pursuant to Minn. Stat. 14.61, the final decision of the Commissioner shall not be made until this Report has been made available to the parties to the proceeding for at least ten days. An opportunity must be afforded to each party adversely affected by this Report to file exceptions and present argument to the Commissioner. Parties should contact Thomas H. Borman, Commissioner, Minnesota Department of Commerce, 133 East Seventh Street, St. Paul, Minnesota 55101, to ascertain the procedure for filing exceptions or presenting argument.

STATEMENT OF ISSUES

The issues in this matter are: (1) Whether the Applicant Bank meets current industry standards of capital adequacy, management quality, and asset condition; (2) Whether the establishment of the proposed detached facility will improve the quality or increase the availability of banking services in the community to be served; and (3) Whether the establishment of the proposed detached facility will have an undue adverse effect upon the solvency of existing financial institutions in the community to be served.

Based upon all of the proceedings herein, the Administrative Law Judge makes the following:

#### FINDINGS OF FACT

1. On August 29, 1990, the Farmers and Merchants State Bank of Balaton submitted an application to establish a detached facility in the City of North Mankato, 500 feet west of the intersection of Commerce Street and Lorrway Drive in North Mankato, Minnesota. The application was formally filed on October 5, 1990. (Ex. 15).

2. On October 15, 1990 a Notice of the Application was published in the Mankato Free Press. On October 18, 1990 a Notice of the Application was published in the Balaton-Russell Press-Tribune-Record. Copies of the notice of the application were also sent by certified mail to the banks located within a three-mile radius of the proposed facility. (Ex. 21).

3. By a letter dated October 30, 1990 and received by the Department of Commerce on October 31, 1990 the Valley National Bank of North Mankato objected to the application and requested a hearing. (Ex. C).

4. On November 9, 1990 the Commissioner of Commerce issued a Notice of and Order for Hearing directing that a contested case hearing be held pursuant to the Administrative Procedure Act on December 18, 1990. The Notice of and Order for Hearing was served upon both the Applicant and the Objector. (Ex. 17). The Notice of and Order for Hearing was published in the Mankato Free Press on November 16, 1990. (Ex. 18).

5. The main office of the Applicant is located at 112 Third Street in Balaton, Minnesota. The Applicant also maintains a branch facility in Tracy, Minnesota which opened in 1982. At present the footings of the bank are approximately \$29 million. The bank has seven employees at its home office and nine at its present detached facility. The Tracy facility presently accounts for approximately 55 percent of the Applicant's deposit base. The Applicant emphasizes agricultural and consumer lending.

6. Although the Applicant experienced some adverse conditions from 1983

to 1985 as a result of the farm depression in Minnesota, it has been profitable since 1986. Its net income rose from \$150,000 in 1986 to \$257,000 in 1989. During the same time period its total assets rose from approximately \$21 million to \$25 million and its net write-off of loans decreased. The average annual return on assets from 1986 through September 30, 1990 was 0.836 percent. (Ex. 16, Tab 2).

7. The Applicant was most recently examined by the FDIC in July of 1990. Its CAMEL rating at that time was two on a scale of one to five with one being the highest rating. (Ex. 13). At the time of the examination approximately \$470,000 in loans of a \$16.5 million portfolio were classified as substandard. The Applicant's capital assets ratio as of September 30, 1990 was 8.52 percent. (Ex. 16, Tab 2).

8. The Applicant has established a community reinvestment act (CRA) statement which sets as a goal providing credit for those of low-moderate-income status. (Ex. 10). It has done so in the Balaton and Tracy communities. The Applicant has been recognized by the Commissioner of Commerce for having at least 60 percent of its deposits in loans during 1988. (Ex. 11).

9 . The Applicant is wholly owned by the Balaton Agency, Inc. which in turn is owned 100 percent by V.G. Schaffer and his family. Mr. Schaffer has been in banking for 51 years, bought the Applicant in 1967 and has seen its assets increase from \$300,000 to \$29 million. He is presently Chairman of the Applicant and is active in managing the Applicant's investment portfolio as well as in some loan decisions.

10. The Applicant's President is Robert P. Reiter, age 51, who has been employed by the Applicant since 1981. From 1969 through 1981, Mr. Reiter was with the Farmers State Bank of Flandreau, South Dakota, and served as Vice-President and as a member of the Board of Directors of that bank from 1974 through April of 1982. (Ex. 1). Mr. Reiter is a high school graduate and has completed several courses in banking, lending and management. (Ex. 1). Mr. Reiter has been an active member of the Chamber of Commerce in both communities served by the Applicant, has served on his church's finance committee, has served on the Board of Directors of the Southwest Initiative Fund and the Tracy Port Authority, as well as the Prairieland Economic Development Corporation. He also is on the Citizen Committee for the U.S. Army National Guard Company in Tracy. (Ex. 2).

11. The Applicant maintains a free checking program, does not charge a fee for check cashing and encourages direct deposits by fixed income people. It has eliminated minimum balance for savings accounts and encourages personal savings by paying 5.5 percent interest which is above that of other banks in the area. It presently has 320 student loans outstanding and has processed 30 Minnesota housing finance agency home improvement loans during 1990. It has also made loans through the Farmers Home Administration, the Rural Finance Authority-and the Small Business Administration-. (Ex. 2).

12. The Applicant seeks to open a second detached facility in the City of North Mankato on Commerce Street near its intersection with Lorrain Drive. The

detached facility would be approximately 95 miles from the Applicant's main office in Balaton. The proposed site is approximately two acres and is located across the street from the Commerce Industrial Park in North Mankato. (Ex. 5).

5). The Applicants have obtained an option to purchase the site at a cost of \$90,000. The option expires on March 10, 1991. (Ex. 6).

6). The site is appropriately zoned for a banking facility. (Ex. 7).

13. The Applicant proposes to build an energy efficient building with approximately 1800 square feet. It would initially have two teller windows and a two-unit drive-up facility. The total cost of land building and furniture and equipment is estimated to be \$350,000. (Ex. 15).

14. The Applicant intends to operate the facility as a full-service bank, offering free checking, savings accounts, certificates of deposit, drafts, money orders, travelers checks, safekeeping facilities, loans and credit cards. Its emphasis in lending would be on consumer loans, real estate loans and financial counseling. It will add an ATM machine if the demand exists. It will consider establishing longer banking hours in order to serve the needs of its customers and employees of the adjacent industrial park.

15. Mark A. Stoffel, who is presently a loan officer with the Applicant, will manage the proposed branch. Mr. Stoffel has a B.S. degree in Business Administration and Management from Southwest State University and has taken courses in bank operations, lending and management. From 1981 to 1986, he was

employed in various capacities with Norwest Bank in Marshall . From 1986 to 1989, he was with the Silver Lake Bank Corporation and served as branch manager of the Magnolia, Minnesota office, Assistant Vice-President at the Luverne, Minnesota office and Executive Vice-President and Director of the First State Bank of Lake Wilson. Mr. Stoffel has been with the Applicant for the past 15 months and serves as the branch manager for the Tracy facility. (Ex. 8).

16. Teresa M. Swanson, who is presently a loan officer trainee with the Applicant, is proposed as the office supervisor for the new facility. She is a high school graduate and a licensed insurance agent. She has been employed by the Applicant since 1979 as an insurance agent, as a manager and as a loan officer trainee. She is currently President of the Balaton Chamber of Commerce and Secretary of the Balaton Lakeside Cemetery. (Ex. 9).

17. The Applicant's President, Robert Reiter will spend two days each week at the proposed North Mankato facility. He will oversee the operation of the proposed facility. Chairman Schaffer will also be available as needed.

18. The Applicant describes the trade territory for the proposed facility as the City of North Mankato and an area approximately ten miles to the north, east and west but excluding the City of Mankato. The trade territory is currently served by only one bank, the Valley National Bank of North Mankato, which also has a branch facility in North Mankato.

19. The population of North Mankato increased from 7,347 people in 1970 to 9,145 people in 1980, to an estimated 10,381 people at present. The housing units in North Mankato increased from 2,309 in 1970 to 3,388 in 1980. A number of industries are located in North Mankato, including Carlson Craft-Specialty Printing with 2,000 employees; Kato Engineering/Reliance Electric with 530 employees; and MICO, Inc., with 271 employees. (Ex. 3). The industrial park adjacent to the proposed site has approximately 3,000 employees. The industrial park, which was started in the mid-1970s, is home to 27 firms. All but 20 acres of the 180-acre park have been sold. (Ex. 4).

20. The Applicant estimates that its total deposits at the end of its first year for the branch facility will total \$3 million, at the end of the second year, \$6 million and at the end of the third year, \$8 million. It estimates that in the first year the proposed facility will have a net loss of \$114,000, in the second year a loss of \$12,000 and in the third year, a profit of \$1,000. The income projections assume an interest rate spread of 4 percent which is what the Applicant is currently experiencing. The estimates are based in part on the Applicant's experience at its detached facility in Tracy, Minnesota. The Tracy facility currently has deposits of \$12.5 million. Tracy is a community of 2,000 people. (Ex. 15).

21. It is projected that the Applicant with its proposed branch would have total average assets of \$31.5 million in 1991 which would increase to approximately \$51 million in the year 2000. During the same time period the capital as a percent of assets is projected to increase from 8.05 percent to 10.48 percent and the dividend payout ratio is expected to decrease from 15.62 percent to 6.5 percent. (Ex. 16, Tab 1).

22. There are four banks located in the trade territory defined by the Applicant. The Valley National Bank of North Mankato has total assets of approximately \$71 million, and a 5-year compound growth rate of 9.1 percent.



Its main office is two miles southeast of the proposed facility and its branch is one-quarter mile east. The First National Bank of St. Peter is located 12 miles north of the proposed facility. It has total assets of approximately \$78 million and a 5-year compound growth rate of 3.6 percent. The Nicollet County Bank of St. Peter is 12 miles north, has total assets of approximately \$55 million and a 5-year compound growth rate of 2.3 percent. The Peoples State Bank of Madison Lake is 15 miles to the east of the proposed facility, has total assets of \$11 million and a 5-year compound growth rate of 0.7 percent. Additionally, there are nine banks or branches and four savings and loan companies in the City of Mankato which are approximately three miles from the proposed branch facility. The five banks located in Mankato have total assets ranging from \$29 million to \$296 million. (Ex. 16, Tab 5). The average 5-year compound growth rate of the eight banks closest to the proposed facility is 3.4 percent. (Ex. 16, Tab 5).

23. The Chairman of the Applicant bank is prepared to assist the bank if the projections for the proposed facility are overly optimistic. He would be willing to reduce his salary, reduce dividends or inject capital as needed. (Ex. 20).

24. The Federal Deposit Insurance Corporation has approved the Applicant's application for the branch facility in question pending approval by the Commissioner of Commerce. (Ex. 12).

Based upon the foregoing Findings of Fact, the Administrative Law Judge makes the following:

#### CONCLUSIONS

1. The Administrative Law Judge and the Commissioner of Commerce have jurisdiction in this matter pursuant to Minn. Stat. 47.54 and 14.50.

2. The notice of filing of the application and notice of the hearing in this matter was proper and timely given, an objection was timely filed, and all

relevant and substantive and procedural requirements of law or rule have been fulfilled.

3. The proposed facility is within 100 miles of the Applicant's principal Office.

4. The proposed facility would be located in a municipality having a population of more than 10,000.

5. The proposed facility would not be closer than 50 feet to any other detached facility or closer than 100 feet to a principal office of any other bank.

6. The Applicant Bank meets current industry standards of capital adequacy, management quality, and asset condition.

7. The establishment of the proposed detached facility will improve the quality or increase the availability of banking services in the community to be served.

8. The establishment of the proposed detached facility will not have an

undue adverse effect on the solvency of existing financial institutions in the community to be served.

9. Any Finding of Fact more properly termed a Conclusion is hereby adopted as such.

Based upon the foregoing Conclusions, the Administrative Law Judge makes the following:

#### RECOMMENDATION

IT IS HEREBY RECOMMENDED that the Commissioner of Commerce approve the application of the Farmers and Merchants State Bank of Balaton to establish a detached facility 500 feet west of the intersection of Commerce Street and Lorrain Drive in the City of North Mankato, Minnesota.

Dated this 27th day of December, 1990.

GEORGE A. BECK  
Administrative Law Judge

#### NOTICE

Pursuant to Minn. Stat. 14-62, subd. 1, the agency is required to serve its final decision upon each party and the Administrative Law Judge by first class mail.

Reported: Taped. Tape Nos. 9382 and 9381.  
No Transcript Prepared.

#### MEMORANDUM

This contested case proceeding is required under Minn. Stat. 47.54, subd. 3. In order to prevail the Applicant in this case must show by a preponderance of the evidence that the three criteria set out in the Statement of Issue and the Conclusions have been satisfied.

The last criteria is that the establishment of the facility in North Mankato will not have an undue adverse effect upon the solvency of existing financial institutions in the community. Generally, the term insolvency means

the inability to pay one's debts in the ordinary course of business. The evidence submitted by the Applicant indicates that the financial institutions in the community are in a healthy condition and that as a group they have shown growth in the past several years. More specifically, the Objector, with total asset in excess of \$71 million, has shown a 5-year compound growth rate over 9 percent. Although the growth rates of the other banks in the proposed trade territory have been less favorable, they are located some ten to twelve miles away and have not filed an objection in this matter. At the hearing the

Objector conceded that there would be no undue adverse effect upon itself or other financial institutions in the community to be served. It is therefore concluded that the Applicant has met its burden of proof to show that there would be no undue adverse effect upon the solvency of existing financial institutions.

The Applicant bank must also show that it meets current industry standards of capital adequacy, management quality and asset condition. The evidence submitted at the hearing indicates that the Applicant is in a strong capital position and has experienced an increasing profitability in the past five years. Its CAMEL rating is a number 2 on a scale of one to five. Its most recent examination by the FDIC was positive. The evidence also indicates that the Applicant has an experienced management team which it can utilize to staff the new facility in a satisfactory manner. At the hearing the Objector conceded that the Applicant's capital levels appeared to be good and that its management quality appeared to be good. However, it made two arguments in regard to this standard. It first suggested that the facility would experience a management problem in that the president of the bank Mr. Reiter would be present at the Facility only two days per week and he might have difficulty doing that because of the distance of 100 miles from the main office to the proposed Facility. However, Mr. Reiter indicated that he would be spending two days per week at the main office, as well as each facility and that he was committed to the hours necessary to see that this would be accomplished. Additionally, the Applicant plans a full-time manager for the branch facility, namely, Mr. Stoffel. The Applicant also indicated that additional employees such as loan personnel will be hired as is necessary and that its Chairman would be on call.

The Objector also argued that the asset condition and capital adequacy might well be affected by what it believes are overly optimistic growth rates

presented by the Applicant. The Objector presented in its Exhibit A what it believes are realistic profit or loss results based on its experience in the community. It projects a growth in assets from \$1.5 million at the end of the first year to \$7.5 million at the end of the fifth year. It predicts that the loss in the first year will amount to approximately \$172,500 and that in the fifth year there will still be a loss of \$11,000. In making its projections the Objector assumed a net interest spread on assets of 3.5 percent as against the 4 percent assumption employed by the Applicant. The Objector also believes that what the Applicant sees as a good growth rate for financial institutions in the entire Mankato area is not quite as rosy when one considers that some of the rates have been augmented by acquisitions by local financial institutions. There is no particular reason to assume that the Objector's projections are more accurate than those of the Applicant. The interest rate spread employed by the Applicant is that which it is currently experiencing. Even if the Objector's figures prove to be more accurate it would be difficult to conclude that the slower growth projected would affect the Applicant's capital adequacy or asset condition so that it would not meet current industry standards. The Chairman of the Applicant has indicated that he stands ready to provide capital to the Applicant should it be necessary to do so.

Finally, the Applicant must show that the establishment of the facility will improve the quality or increase the availability of banking services in the community. The Findings of Fact reflect the services which the Applicant expects to provide in North Mankato. There may be some improvements in services in that the Applicant offers free checking and in that its banking

hours may be more convenient. The Objector argues that the true trade area in regard to this facility is the entire Mankato area which would include a large number of banking and other financial offices located in the City of Mankato, which is a city of approximately 30,000 people. It suggests that the some 30 financial offices in the area are adequate to serve existing needs. (Ex. B). The Applicant points out however that a second banking facility in North Mankato will improve the competitive situation to the benefit of consumers. it points out that a small town, people driven bank with emphasis on consumer loans will add a different service to the community. Additionally, the location immediately adjacent to the Industrial Park together with extended banking hours and employing an ATM machine will be enhanced facilities for the community. It is concluded that Applicant has demonstrated by a preponderance of the evidence that it will increase the availability of banking services in North Mankato and the adjacent trade area.

G.A.B.